



12 CFR Parts 614, 615, 620, and 628

RIN 3052-AD27

Regulatory Capital Rules: Tier 1/Tier 2 Framework

AGENCY: Farm Credit Administration.

ACTION: Final rule.

SUMMARY: The Farm Credit Administration (FCA or we) is adopting a final rule that amends the regulatory capital requirements for Farm Credit System (System or FCS) institutions. These amendments clarify certain provisions in the Tier 1/Tier 2 Capital Framework final rule that became effective in 2017 (2017 Capital Rule) and codify the guidance provided in FCA Bookletter - BL-068 - Tier 1/Tier 2 Capital Framework Guidance. This final rule also includes revisions to the regulatory capital rules to reduce administrative burden for System institutions and the FCA. Lastly, to maintain comparability in our regulatory capital requirements, we are amending certain definitions pertaining to qualified financial contracts in conformity with changes adopted by the Federal banking regulatory agencies.

DATES: The regulation shall become effective January 1, 2022, or 30 days after publication in the *Federal Register* during which either or both houses of Congress are in session, whichever is later. Pursuant to 12

U.S.C. 2252(c)(1), FCA will publish notification of the effective date in the *Federal Register*.

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I. Introduction

A. Objectives of the Final Rule

FCA's objectives in adopting this rule are to:

- Provide technical corrections, amendments and clarification to certain provisions in the Tier 1/Tier 2 Capital Framework; and
- Ensure the System's capital requirements maintain comparability with the standardized approach that the Federal banking regulatory agencies¹ have adopted (U.S. Rule) while accommodating the cooperative structure and the organization of the System.

B. Background

In 1916, Congress created the System to provide permanent, stable, affordable, and reliable sources of credit and related services to American agricultural and aquatic producers.² As of June 30, 2021, the System consists of 3 Farm Credit Banks, 1 agricultural credit bank, 66 agricultural credit associations, 1 Federal land credit association, service corporations, and the Federal Farm Credit Banks Funding Corporation (Funding Corporation). Farm Credit banks (including both the Farm Credit Banks and the agricultural credit

¹ The Federal banking regulatory agencies are the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), and the Board of Governors of the Federal Reserve (FRB). See 12 CFR 3.20(b)(1)(i) (OCC), 12 CFR 324.20(b)(1)(i) (FDIC); 12 CFR 217.20(b)(1)(i) (FRB).

² The Federal Agricultural Mortgage Corporation (Farmer Mac), which is also a System institution, has authority to operate secondary markets for agricultural real estate mortgage loans, rural housing mortgage loans, and rural utility cooperative loans. The FCA has a separate set of capital regulations that apply to Farmer Mac. This rulemaking does not affect Farmer Mac, and the use of the term "System institution" in this preamble and rule does not include Farmer Mac.

bank) issue System-wide consolidated debt obligations in the capital markets through the Funding Corporation,³ which enable the System to extend short-, intermediate-, and long-term credit and related services to farmers, ranchers, aquatic producers and harvesters, their cooperatives, rural utilities, exporters of agricultural commodities products, farm-related businesses, and certain rural homeowners.⁴ The System's enabling statute is the Farm Credit Act of 1971, as amended (Act).⁵

FCA's Tier 1/Tier 2 Capital Framework, the 2017 Capital Rule, was published in the *Federal Register* in July 2016.⁶ The objectives of the 2017 Capital Rule were:

- To modernize capital requirements while ensuring that institutions continue to hold enough regulatory capital to fulfill their mission as a Government-sponsored enterprise (GSE);
- To ensure that the System's capital requirements are comparable to the Basel III framework and the

³ The Funding Corporation was established pursuant to section 4.9 of the Farm Credit Act of 1971, as amended, and is owned by all Farm Credit banks.

⁴ The agricultural credit bank lends to and provides other financial services to farmer-owned cooperatives, rural utilities (electric and telecommunications), and rural water and wastewater disposal systems. It also finances U.S. agricultural exports and imports and provides international banking services to cooperatives and other eligible borrowers. The agricultural credit bank operates a Farm Credit Bank subsidiary.

⁵ 12 U.S.C. 2001-2279cc. The Act is available at www.fca.gov under "Laws and regulations" and "Statutes."

⁶ 81 FR 49720 (July 28, 2016). The rule was effective January 1, 2017.

standardized approach in the U.S. Rule, but also to ensure that the rules take into account the cooperative structure and the organization of the System;

- To make System regulatory capital requirements more transparent; and
- To meet the requirements of section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act).⁷

To date, FCA believes the 2017 Capital Rule has met, and continues to meet, these stated objectives.⁸

On December 22, 2016, the FCA Board adopted FCA Bookletter - BL-068 - Tier 1/Tier 2 Capital Framework Guidance (Capital Bookletter).⁹ The Capital Bookletter provided guidance to ensure System institutions had the necessary information to correctly implement the requirements of the 2017 Capital Rule. The Capital Bookletter included clarification and technical fixes on 18 separate items. The Capital Bookletter also stated our intention to incorporate some of these items into the regulation in a future rulemaking project.

C. Summary of the Proposed Rule

⁷ Public Law 111-203, 124 Stat. 1376 (2010).

⁸ For a comprehensive discussion of the 2017 Capital Rule, see 81 FR 49720 (July 28, 2016). FCA's capital requirements can be found at Parts 615 and 628 of FCA Regulations.

⁹ A copy of the Capital Bookletter can be found at www.fca.gov, under "Laws & Regulations" and "Bookletters."

On September 10, 2020,¹⁰ FCA published in the *Federal Register* a notice of proposed rulemaking seeking public comment on revisions to our regulatory capital requirements to incorporate some of the guidance in the Capital Bookletter, with various adjustments,¹¹ as well as other revisions, as follows:

- Eliminate the stand-alone capital requirements for Farm Credit Leasing Services Corporation (Farm Credit Leasing or FCL);
- Change the computation of the lending and leasing limit base in § 614.4351, by using total capital instead of permanent capital in the calculation¹² and eliminating the exceptional treatment of certain purchased stock in § 614.4351(a)(1);
- Simplify "Safe Harbor" provisions that determine when System institutions have "deemed prior approval" from FCA to distribute cash payments;
- Revise and clarify certain criteria that capital instruments must meet to be included in common equity tier 1 (CET1) and tier 2 capital;

¹⁰ See 85 FR 55786 (September 10, 2020).

¹¹ FCA adjusted some of the guidance provided in the Capital Bookletter to address concerns identified through ongoing monitoring and examination of the requirements of the 2017 Capital Rule. Specific elements of the Capital Bookletter as incorporated into the rule are detailed in the "Substantive Revisions" and the "Clarifying and Other Revisions" sections of this preamble.

¹² Total capital is defined at § 628.2. Permanent capital is defined at § 615.5201.

- Further clarify when the holding period starts for certain Common Cooperative Equities included in CET1 or tier 2 capital; and
- Amend the requirement to adopt an annual board resolution with respect to prior approval requirements and the minimum holding periods for certain equities included in CET1 or tier 2 capital.

We additionally proposed technical revisions to:

- Amend the definitions of "Collateral agreement," "Eligible margin loan," "Qualifying master netting agreement (QMNA)," and "Repo-style transaction" to incorporate amendments made to these definitions in the U.S. Rule;
- Amend § 615.5220(a)(6) to replace references to parts 615 and 628 with a general reference to FCA regulations;
- Make certain amendments to § 620.5 to ensure institutions report financial information as we intended;
- Clarify the appropriate risk-weighting of cash and gold bullion held in a System institution's own vaults;
- Correct securitization formulas as provided in the Capital Bookletter;

- Specify the deductions and adjustments required for calculating the requirement in § 628.10 that at least 1.5 percent of the 4 percent tier 1 leverage ratio minimum must consist of unallocated retained earnings (URE) and URE equivalents;
 - Revise the deductions required under existing § 628.22(a)(6) to include allocated equity investments in System service corporations;
 - Add to the regulation certain guidance in the call report instructions on the treatment of accruals of patronage or dividend payables or receivables recorded prior to the governing board declaration or resolution;
 - Clarify certain requirements for regulatory capital disclosures of System banks in §§ 620.3, 628.62(c), and 628.63(b)(4); and
 - Clarify that institutions may retire minimum amounts of statutory borrower stock without prior approval from FCA so long as, after the retirement, the institution continues to comply with all minimum regulatory capital requirements.
- The proposal also provided clarification and guidance on continuously redeemable preferred stock (or "H Stock"), responded to a letter received from the Farm Credit Council addressing various capital related topics, and sought comment

on potential changes to FCA's existing permanent capital regulations.

D. General Summary of Comments Received

FCA received seven comment letters on the proposed rule.¹³ The Farm Credit Council, a trade association representing System institutions, submitted a letter on behalf of its membership after soliciting comments from all institutions (System Comment Letter).¹⁴ Two System banks¹⁵ and three System associations¹⁶ also submitted individual comment letters in support of the System Comment Letter. One System association, Compeer Financial, ACA (Compeer), raised additional concerns. The American Bankers Association (ABA), a trade association representing the U.S. banking industry, submitted the remaining comment letter.¹⁷ We address the comments in the preamble sections that follow.

The System Comment Letter stated that the Farm Credit Council and its members "generally support" the

¹³ The comment letters for the proposed rule are available at www.fca.gov. Once you are on the website, click the "I want to..." field near the top of the page; select "find comments on a pending regulation" from the drop down menu; and click "Go;" then select Capital - Tier 1/Tier 2 Capital Framework - Clean Up - NPRM.

¹⁴ See Letter from Charles Dana, General Counsel, Farm Credit Council (November 6, 2020).

¹⁵ See Letter from Thomas E. Halverson, President and Chief Executive Officer, CoBank, ACB (November 9, 2020); Letter from Barbara Kay Stille, Chief Administrative Officer and General Counsel, AgriBank, FCB (November 9, 2020).

¹⁶ See Letter from Northwest Farm Credit Services, FLCA and PCA (November 6, 2020); Letter from Steve Zagar, Senior Vice President Chief Financial Officer, Farm Credit Mid-America, ACA (November 9, 2020); Letter from Jase Wagner, Chief Financial Officer (CFO), Compeer Financial, ACA (November 5, 2020).

¹⁷ See Letter from Hu A. Benton, Vice President, Banking Policy, American Bankers Association (November 9, 2020).

proposed rule, including provisions that incorporate the Capital Bookletter and call report instructions, but that certain aspects of the proposal were “problematic.” Many of the comments from System institutions reiterated recommendations they had previously communicated to FCA (in comments on the September 4, 2014, proposed rulemaking)¹⁸ and requested changes that were beyond the scope of the proposal. The balance of the comments from System institutions were supportive of the proposed amendments or requested specific technical changes.

The ABA asserted that the proposed rule would increase risks to the safety and soundness of the System and increase competitive inequities between the System and commercial banks. The ABA also requested that we clarify certain matters we did not expressly address in the proposal. In some cases, the ABA’s comments did not directly relate to the amendments we proposed.

In the preamble to the proposed rule, we discussed certain matters that were not the subject of the proposed rule,¹⁹ and we also sought comments on potential changes to our permanent capital regulations

¹⁸ See 79 FR 52814 (September 4, 2014).

¹⁹ In the proposed rule preamble, we discussed the exclusion of continuously redeemable preferred stock (H Stock) from tier 1 and tier 2 capital and also commented on issues raised in a 2016 letter we received from the Farm Credit Council. See 85 FR 57786, 55795 (September 10, 2020).

to reduce regulatory burden. We may consider proposing specific changes to the permanent capital requirements and calculations in a future rulemaking.

As discussed in Section 2 - Substantive Revisions to the Capital Rule and Section 3 - Clarifying and Other Revisions to the Capital Rule, the final rule adopts the revisions we proposed with minor adjustments in response to comments received.

II. *Substantive Revisions to the Capital Rule*

A. Safe Harbor Deemed Prior Approval

Under existing § 628.20(f), System institutions are required to obtain prior approval from FCA before retiring equities included in tier 1 or tier 2 capital and making cash payments for dividends and patronage (collectively, cash distributions). Institutions have “deemed prior approval” from FCA for such distributions provided the conditions in § 628.20(f)(5) and (6) are satisfied (Safe Harbor). One of the conditions stipulates that, after any such cash payment, the dollar amount of CET1 capital must equal or exceed the dollar amount of CET1 on the same date in the previous calendar year.²⁰ Using the same date in the previous calendar year has made monitoring and enforcing this

²⁰ See existing regulation § 628.20(f)(5)(ii). FCA considers the date of the cash distribution to be the date on which the institution’s board passes a binding resolution declaring an amount it will make as a cash dividend or patronage refund. This either must be a specified dollar amount or must include language whereby a specific amount can be calculated.

requirement difficult because regulatory capital numbers for System institutions are reported to FCA quarterly, rather than daily.

We proposed to simplify the Safe Harbor provisions of § 628.20(f) by replacing the requirement to use the exact calendar date of the cash distribution with a requirement to use the quarter-end date of the quarter in which the cash payment is made. A System institution would have “deemed prior approval” from FCA if, after making the cash distribution, the dollar amount of CET1 capital at the quarter-end equals or exceeds the dollar amount of CET1 capital on the same quarter-end in the previous calendar year. We provided two examples in the preamble to the proposed rule.²¹ We stated that we do not believe the amendment as proposed would increase or decrease the amount of cash patronage System institutions would be able to pay when compared to the provision in the 2017 Capital Rule.

The ABA expressed concern that the proposal was “liberalizing” the provisions of the “Safe Harbor Deemed Prior Approval” in § 628.20(f)(5) and suggested that the Safe Harbor framework gives inadequate consideration to an institution’s risk profile. The comments appear to be based in part on concerns regarding the proposal’s omission of specific reference

²¹See 85 FR 55786, 55788 (September 10, 2020).

to capital distribution limitations already in the 2017 Capital Rule and unchanged by the proposal.

We disagree with the assertion that the proposal would "liberalize" the Safe Harbor. The proposed rule would change the date for determining compliance with the Safe Harbor provision in order to simplify the administration, enforcement, and monitoring of compliance with the Safe Harbor requirements. As we state above, we do not believe the proposal would increase or decrease the amount of cash patronage System institutions could pay when compared to the existing provision. The proposed changes would in no way "liberalize" the Safe Harbor or create any greater opportunity for capital distributions under the Safe Harbor.

In response to the ABA's concerns regarding the Safe Harbor giving inadequate consideration to an institution's risk profile, the commenter's assertion that the Safe Harbor permits "cash payouts based only on maintaining the dollar amount of CET1 capital in a prior year" is incorrect. As we stated in the preamble to the proposed rule, in order to make a cash distribution under the Safe Harbor, a System institution must remain in compliance with all regulatory capital requirements and any supervisory or

enforcement actions after such distribution.²² FCA's regulatory capital requirements are comparable to the U.S. Rule and include regulatory capital measures using both risk-adjusted and non-risk-adjusted computational methods.²³ Furthermore, FCA has comparable authorities to the Federal banking regulatory agencies to establish minimum capital ratios for an individual institution²⁴ as well as to place further restrictions on institutions' capital distributions as part of supervisory agreements and enforcement actions.²⁵ Lastly, cash distributions under the Safe Harbor are subject to the capital buffers in § 628.11, which reduce the amount of capital distributions an institution can make when its capital levels fall within the leverage buffer or capital conservation buffer ranges. These requirements are unaltered by the proposed or final rule.

Compeer requested that we expand the Safe Harbor to allow institutions to retire the allocated equities of a borrower, irrespective of compliance with minimum holding periods,²⁶ to offset losses when a borrower

²² See § 628.20(f)(5)(iii).

²³ Compare, for example, §§ 628.10 and 628.11 with the OCC's rules at 12 CFR 3.10 and 3.11.

²⁴ Section 4.3(a) of the Act (12 U.S.C. 2154) and 12 CFR 615.5350.

²⁵ Section 5.25 of the Act (12 U.S.C. 2261).

²⁶ To be included in regulatory capital, common cooperative equities (defined at § 628.2) must meet minimum holding periods as stipulated in § 628.20(b)(1)(xiv) and (d)(1)(xi). Minimum holding period requirements are further discussed below under Section II, C - Common Cooperative Equity Issuance Date.

defaults on a loan. The commenter asserted that present hurdles to retiring equities in these scenarios (i.e., requesting prior approval from FCA under § 628.20(f)) present an unnecessary administrative burden.

Compeer's requested revision is beyond the scope of the present rulemaking. We note, however, that as we stated in the preamble to the 2017 Capital Rule, equities are issued to capitalize the institution, not the loan. Accordingly, these equities should not be viewed or treated as compensating loan balances.²⁷ Furthermore, the preamble to the 2017 Capital Rule also explains in detail our position on the necessity for minimum holding periods to address the "expectation criterion" in the Basel III Framework and the U.S. Rule, maximizing comparability of our rule with the rules applicable to commercial banks.²⁸ We note that, under § 628.20(f)(6), System institutions may offset allocated equities against a loan in default if mandated by a court of competent jurisdiction or under § 615.5290 in connection with a restructuring plan.

The balance of comments received supported this proposed amendment, and we are adopting it as proposed.

B. Capital Bylaw or Board Resolution to Include Equities in Tier 1 and Tier 2 Capital

²⁷ See 81 FR 49720, 49731 (July 28, 2016).

²⁸ See 81 FR 49720, 49732 (July 28, 2016).

The 2017 Capital Rule stipulates conditions and criteria that must be met in order to include an instrument in an institution's regulatory capital.²⁹ Among these are the requirements for the institution's board of directors to affirm its commitment to adhere to the regulatory minimum redemption or revolvment periods; to obtain prior approval from FCA prior to redeeming, revolving, redesignating, cancelling or removing equities included in regulatory capital;³⁰ and to obtain prior approval from FCA for certain other actions that could impact the institution's capital quantity or quality.³¹ Such affirmation must be set forth in the institution's capitalization bylaws or in a board resolution that the board must re-affirm annually. Where this requirement is satisfied by a board resolution, we proposed to reduce the administrative burden by no longer requiring an annual re-affirmation by the board. We proposed to replace the annual re-affirmation with a one-time requirement to adopt the board resolution and, in subsequent annual

²⁹ See existing regulations §§ 628.20 and 615.5200(d).

³⁰ By meeting the conditions for "deemed prior approval" under regulation § 628.20(f)(5) and (6), an institution effectively obtains FCA prior approval for a given capital distribution.

³¹ Existing § 615.5200(d)(3) requires boards to obtain prior approval before redesignating unallocated retained earnings (URE) equivalents as redeemable equities; removing equities from regulatory capital (other than through repurchase, cancellation, redemption, or revolvment); or redesignating equities from one regulatory capital component to another. Section 615.5200(d)(4) requires that URE equivalents shall not be revolved, except under very limited circumstances (i.e., upon dissolution or liquidation).

capital adequacy plans, to expressly acknowledge the continuing and binding effect of this resolution.

We proposed to move the existing requirements of § 615.5200(d) to a new section, § 628.21, and to revise them to provide that an institution's board must adopt either a capitalization bylaw requirement or a binding board resolution. New § 615.5200(b) would add to existing capital planning provisions a requirement that the capital adequacy plan must expressly acknowledge the continuing and binding effect of all board resolutions adopted pursuant to §§ 628.20(b)(1)(xiv), (c)(1)(xiv), and (d)(1)(xi) and 628.21. We proposed conforming changes as necessary to refer to new § 628.21 rather than §615.5200(d).

We received no specific comments on this amendment and are adopting it as proposed.

C. Common Cooperative Equity Issuance Date

Common cooperative equities³² included in CET1 capital have a minimum holding period of 7 years before redemption or revolvment, and common cooperative equities included in tier 2 capital have a minimum holding period of 5 years.³³ These holding periods also must be met for equities (other than the statutory borrower stock minimum) to be retireable under the Safe Harbor. To clarify when the minimum redemption and

³² Common cooperative equities are defined in § 628.2.

³³ As established in § 628.20(b)(1)(xiv)(A) and (d)(1)(xi)(A).

revolvement period starts for a common cooperative equity, we proposed to add a new definition, common cooperative equity issuance date, in § 628.2 and to make conforming changes to other sections of the regulations. Similar to our guidance in the Capital Bookletter, we proposed to define the common cooperative equity issuance date as the quarter-end in which an institution recognizes newly issued purchased stock in its financial statements and, for newly allocated equities, the quarter-end in which the institution's board has declared a patronage refund and the applicable accounting treatment has taken place. We provided examples of the proposed treatment in the proposed rule preamble.³⁴

The System Comment Letter and Compeer requested that we eliminate altogether the minimum holding period requirements for allocated equities. The System made the same request and supporting arguments in comments on our 2014 Tier 1/Tier 2 proposed capital rule, and FCA responded to those comments in the final rule preamble to the 2017 Capital Rule.³⁵

The System's request not only is beyond the scope of this rulemaking but also presents no new arguments that would persuade us to reevaluate the need for

³⁴ See 85 FR 55786, 55789 (September 10, 2020).

³⁵ See 81 FR 49720, 49732 (July 28, 2016). The proposed rule is at 79 FR 52814 (September 4, 2014).

minimum holding periods. We discussed at length the stock-like attributes of allocated equities (as distinct from unallocated retained earnings) and the reasons for the minimum holding periods in the preamble to the 2017 Capital Rule.³⁶

The System Comment Letter suggested we add the word “calendar” before “quarter-end” in the proposed definition of “common cooperative equity issuance date” to clarify that the issuance date would be the calendar quarter-end. We agree and have incorporated the suggestion into the final rule. FCA also fully acknowledges the legal stock issuance date may be different from the quarter-end date used for financial reporting and regulatory capital calculations. Beyond this minor change, we are adopting the new definition as proposed.

D. Farm Credit Leasing Services Corporation

The proposed rule would recognize the current ownership status of Farm Credit Leasing as a wholly-owned subsidiary of CoBank, ACB (CoBank) by removing FCL from the definition of “System institution” in §§ 615.5201 and 628.2 for the purposes of the regulatory capital requirements.³⁷ In so doing, FCA would no

³⁶ See 81 FR 49720, 49726-49730 (July 28, 2016).

³⁷ Farm Credit Leasing is a service corporation chartered under section 4.25 of the Act. A service corporation is an institution of the System that is established by System banks or associations and chartered by FCA, and it is subject to FCA regulation and examination. See title IV, subpart E of the Act.

longer require FCL to meet minimum capital and related regulatory requirements under part 615, subpart H, and part 628 of our regulations on a stand-alone basis. As a wholly-owned subsidiary of CoBank, FCL is a business unit of the bank with profits and losses accrued to the bank, and its assets and liabilities are consolidated with the bank's assets and liabilities for financial and regulatory reporting purposes. To the extent the bank is adequately capitalized overall, CoBank's consolidation ensures FCL's assets are adequately capitalized. This amendment will reduce the administrative burden of separately applying the regulatory capital requirements to FCL and will not reduce the capital to be held against FCL and CoBank's combined assets. If FCL's ownership status were to change in the future, we will reassess whether to separately apply our regulatory capital requirements.³⁸

Commenters supported this change, and we are adopting it as proposed.

E. Lending and Leasing Limit Base Calculation

Since adopting the 2017 Capital Rule, FCA has relied on tier 1 and tier 2 capital, not on permanent capital, to evaluate the safety and soundness of System institutions. In order to better align the lending and

³⁸ The definitions of "System institution" under §§ 615.5201 and 628.2 provide that we may include "any other institution chartered by the FCA that we determine should be included for purposes of this subpart."

leasing limit base with FCA's supervisory focus on tier 1 and tier 2 capital, we proposed to shift the base of the lending and leasing limit from permanent capital³⁹ to total capital as defined and adjusted in §§ 628.20-628.22 and to continue to include otherwise eligible third-party capital that must be excluded under § 628.23. We further proposed to align the treatment of investments in other System institutions under the lending and leasing limit base with the treatment under regulatory capital calculations by eliminating the exceptional treatment of stock purchased in connection with a loan participation under § 614.4351(a)(1).⁴⁰ We estimated that the impacts to lending limits at System institutions resulting from these changes would be small.⁴¹ The System Comment Letter supported the change to the use of total capital as the lending limit base and noted that most institutions have internal lending limit policies that are lower than the lending limit base in the regulation. We received no other comments and are adopting the amendment as proposed.

³⁹ The existing lending and leasing limit base (which this final rule is changing) is a System institution's permanent capital with adjustments applicable to the institution in accordance with § 615.5207, and with two additional adjustments in § 614.4351(a) that apply only to the lending and leasing limit base.

⁴⁰ The 2017 Capital Rule requires System institutions to deduct their investments in other System institutions from regulatory capital calculations. Existing § 614.4351(a)(1) directs a System institution to include its investment in another System institution in its lending limit base where the investment resulted from stock purchased in connection with a loan participation. This is, in effect, the exact opposite of the regulatory capital requirements in the 2017 Capital Rule.

⁴¹ See 85 FR 55786, 55790 (September 10, 2020), footnotes 29 and 30.

F. Qualified Financial Contract (QFC) Related Definitions

In 2017, the Federal banking regulatory agencies adopted rules establishing certain restrictions and requirements for the financial contracts (QFC Rules) of global systemically important banking institutions (GSIBs).⁴² We provided details on the background and impetus for these regulatory changes in the preamble to the proposed rule.⁴³ The QFC Rules prompted related definitional changes in the U.S. Rule to ensure regulated entities continued to benefit from recognition of the risk-mitigating effects of netting and financial collateral on certain financial transactions. This recognition likely results in reduced capital requirements for those transactions.

To incorporate amendments made to the U.S. Rule⁴⁴ and to ensure System institutions would also continue to benefit from recognition of the risk-mitigating effects of netting and financial collateral, we proposed changes to the definitions of "Collateral agreement," "Eligible margin loan," "Qualifying master netting agreement (QMNA)," and "Repo-style transaction." The proposed changes to QMNA would also

⁴² See 82 FR 56630 (November 29, 2017) (OCC); 82 FR 50228 (October 30, 2017) (FDIC); and 82 FR 42882 (September 12, 2017) (FRB).

⁴³ See 85 FR 55786, 55790-55791 (September 10, 2020).

⁴⁴ As we have previously stated, FCA seeks to achieve comparability between our regulatory capital rules and those of the Federal banking regulatory agencies. Among other benefits, comparability of rules increases transparency for investors in the capital markets.

harmonize that definition with the definition of “Eligible master netting agreement” as used in FCA’s Margin and Capital requirements for Covered Swap Entities regulation.⁴⁵ The System Comment Letter supported these revisions, and we are adopting them as proposed.

G. Common Equity Tier 1 Capital Eligibility Requirements

Consistent with the Basel III regulatory capital framework⁴⁶ and the U.S. Rule, we proposed to add the term “paid-in” to the eligibility criteria for CET1 capital in § 628.20(b)(1)(i). Basel III defines “paid-in” capital as capital that (1) has been received with finality by the institution, (2) is reliably valued, (3) is fully under the institution’s control, and (4) does not directly or indirectly expose the institution to the credit risk of the investor.⁴⁷

As discussed in the preamble to the proposed rule, we proposed this amendment to the eligibility criteria for CET1 capital after re-evaluating the attributes of System allocated equities, which we have subsequently determined meet the Basel definition of “paid-in.”⁴⁸ We further discussed our reexamination of the attributes

⁴⁵ See § 624.2.

⁴⁶ See Basel Committee on Banking Supervision (BCBS), Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems, December 2010 (as revised June 2011).

⁴⁷ See BCBS, Basel III Definition of capital – Frequently Asked Questions, September 2017 (update of FAQs published in December 2011).

⁴⁸ See 85 FR 55786, 55791-55792 (September 10, 2020).

of allocated equities and the financing of statutorily required borrower stock at System institutions.⁴⁹ The System Comment Letter supported our recognition of allocated equities as meeting the definition of “paid-in” and expressed no concern with the additional criteria for an instrument’s inclusion in CET1 capital.⁵⁰ We are adopting the revision as proposed.

We also proposed a conforming change in § 628.20(d)(1)(i) to clarify that all instruments included in tier 2 capital must be issued and paid-in. We received no comments on this proposed change and are adopting it as proposed.

Lastly, we proposed clarifying, non-substantive changes to § 628.20(b)(1)(i) and (b)(1)(ii), both to align our language more closely with the language in the U.S. Rule and to emphasize a difference between the rules’ prioritization of a capital instrument holder’s claim on the residual assets of an institution in a receivership, insolvency, liquidation, or similar proceeding. We received no comments on these proposed revisions and are adopting them as proposed.

III. Clarifying and Other Revisions to the Capital Rule

⁴⁹ Id.

⁵⁰ As discussed under Section III, E – Unallocated Retained Earnings and Equivalents Deductions and Adjustments, the System Comment Letter draws a connection between our determination that allocated equities are “paid-in,” as defined by the Basel Committee, and arguments in the letter requesting the elimination of the URE and URE equivalents requirements in FCA’s capital rules. Our determination that allocated equities fully meet the Basel III definition of paid-in capital does not have any connection to our URE and URE equivalents requirements.

A. Capitalization Bylaw Adjustment

Section 615.5220(a)(6) requires a System institution to include in its capitalization bylaws a provision stating that equities other than those protected under Section 4.9A of the Act are retireable at the sole discretion of the board, provided minimum capital adequacy standards established in subpart H of part 615 and part 628 are met. We proposed to amend this section by replacing the reference to parts 615 and 628 with a general reference to FCA's capital adequacy standards. This would satisfy the requirement to refer to parts 615 and 628 and would include all existing capital requirements of the FCA as well as any future capital requirements that we may adopt in other parts of our regulations.

As we noted in the proposal,⁵¹ changes to bylaws to conform to this regulatory requirement should not change any substantive rights of the System institution or its member-borrowers.⁵² System institutions that have already amended their capitalization bylaws to include a reference to parts 615 and 628 do not need to amend their capitalization bylaws to comply with this revision.

⁵¹ See 85 FR 55786, 55792 (September 10, 2020).

⁵² If the change is non-substantive and does not alter, reduce, or increase the rights of any member-borrowers, a System institution's board may choose to make a conforming change to the capitalization bylaws to include a general reference to regulatory capital adequacy standards without a vote by its member-borrowers, provided that such bylaws allow for technical amendments without a shareholder vote.

We received no comments on this amendment and are adopting it as proposed.

B. Annual Report to Shareholders Corrections

We proposed technical revisions to § 620.5, which lists the required contents of a System institution's annual report to shareholders, to ensure institutions report financial data as we intended. First, we proposed to move the requirement that System associations report their tier 1 leverage ratio in each annual report for each of the last 5 fiscal years from § 620.5(f)(4)(iv) to § 620.5(f)(3)(v), as we had originally intended. In addition, we proposed to amend the requirement in § 620.5(f)(4) that institutions report core surplus, total surplus, and the net collateral ratio (banks only) in a comparative columnar form for each fiscal year ending in 2012 through 2016. This requirement resulted in System institutions reporting capital ratios beyond the 5-year requirement established in § 620.5(f), which was not our intention. Accordingly, we proposed to require these disclosures in each annual report through 2021, but only as long as these ratios are part of the previous 5 fiscal years for which disclosures are required. We received no comments on these revisions and are adopting them as proposed.

C. Appropriate Risk-Weighting of Cash and Gold

Bullion

We proposed to delete provisions in § 628.32(1)(1) pertaining to the risk weighting of cash that were redundant and potentially confusing. Specifically, existing § 628.32(1)(1) states that System institutions must assign a 0-percent risk weight to cash held in accounts at a depository institution, which created potential confusion pertaining to the proper risk weight for deposits that exceed the limit of FDIC deposit insurance coverage (currently set at \$250,000). In addition, existing § 628.32(1)(1) also states that System institutions must assign a 0-percent risk weight to cash held in accounts at a Federal Reserve Bank. As the risk weighting of cash on deposit with a U.S. depository institution or at the Federal Reserve Bank is adequately and more accurately addressed in § 628.32(a)(1)(i)(A) and (B) and (d)(1), we proposed eliminating the duplicative and potentially confusing provisions in § 628.32(1)(1). We received no comments on these revisions and are adopting them as proposed.

We additionally proposed to revise § 628.32(1)(1) to add a provision assigning a 0-percent risk weight to gold bullion held in a System institution's own vaults, consistent with the risk weight assigned to gold bullion held in the vaults of a depository institution.

We received no comments on this revision and are adopting it as proposed.

D. Securitization Formulas

Consistent with corrections previously provided in the Capital Bookletter, we proposed to correct 3 formulas used in the simplified supervisory formula approach (SSFA) to risk-weighting securitizations under § 628.43(d), and one formula used in the simple risk-weight approach (SRWA) for risk-weighting equity exposures under § 628.52. These formulas were printed incorrectly in the Federal Register version of the 2017 Capital Rule. We received no comments on these corrections and are finalizing them as proposed.

E. Unallocated Retained Earnings and Equivalents Deductions and Adjustments

Under § 628.10, at least 1.5 percent of the 4 percent tier 1 leverage ratio minimum must consist of URE and URE equivalents (UREE). As the 2017 Capital Rule did not specify how to calculate this requirement, we proposed to prescribe the calculation methodology. Specifically, we proposed to incorporate the guidance in the Capital Bookletter requiring the deductions in § 628.22(a) from the numerator and the deductions used in calculating the tier 1 leverage ratio from the denominator.⁵³ We also proposed to require that

⁵³ See Capital Bookletter, Item 4.

institutions deduct from the numerator any purchased equity investments that must be deducted under the corresponding deduction approach in § 628.22(c). The use of differing deductions for the computation of the tier 1 leverage ratio and the URE and UREE measure, which is a component of the tier 1 leverage ratio, resulted in the URE and UREE measure, when calculated on a stand-alone basis, exceeding the tier 1 leverage ratio at many System institutions.⁵⁴ This was not our intent. The System Comment Letter generally supported our proposed revisions, and we are adopting them as proposed.

In addition, we are adopting technical conforming amendments in § 628.10(c)(4) to incorporate adjustments required under proposed § 628.22(b)⁵⁵ into the computation of both the tier 1 leverage ratio and the URE and UREE measure. More specifically, we are amending the calculation of average total consolidated assets described in § 628.10(c)(4)(i) to include the deduction or adjustment required by § 628.22(b).

⁵⁴ Section 628.10(c)(4) requires the amounts deducted under §§ 628.22(a) and (c) and 628.23 to be deducted from tier 1 capital when calculating the tier 1 leverage ratio. However, the deductions under §§ 628.22(c) and 628.23 were not applied to the numerator when calculating the URE and UREE requirement as they do not increase the URE of a System institution. Although we are amending the rule to incorporate deductions under new § 628.22(b) and existing § 628.22(c), we did not find it necessary to require the deductions under § 628.23 when calculating the URE and UREE measure because third-party stock is not a component of URE, UREE, or CET1 capital.

⁵⁵ Proposed § 628.22(b) is discussed below under Section III, G - Adjustments for Accruing Patronage and Dividends.

Furthermore, we are amending the calculation of the URE and UREE measure described in § 628.10(c)(4)(ii) to include the deduction or adjustment required by § 628.22(b). These conforming changes are consistent with existing call report instructions,⁵⁶ are technical in nature, and are necessary to maintain consistency in the deductions for the computation of the tier 1 leverage ratio and the URE and UREE measure, consistent with the intent of the proposed rule.

The System Comment Letter advocated that FCA reconsider the necessity of requirements to hold a minimum level of URE. Consistent with its comments on our 2014 proposed Capital Rule, the System Comment Letter asserted that the minimum URE requirement establishes URE as higher quality capital relative to other System capital components, results in nearly 3 percent of URE held against each dollar of new loans made by associations, violates the cooperative principle of user-ownership, and undermines the cooperative principle of user-control.⁵⁷ In addition, the System Comment Letter asserted that a minimum URE requirement is not consistent with the Basel III

⁵⁶ See the call report instructions for Uniform Call Report schedule RC-R.4, item 3, and schedule RC-R.5, item 1.c. The call report instructions are available at <https://ww3.fca.gov/fcsinfo/CRS/CallReportFiles/UCR%20Report%20Instructions.pdf>.

⁵⁷ The Farm Credit Council made similar comments in response to the 2017 Capital Rule, as we summarized in the rule's preamble. See 81 FR 49720, 49733-49735 (July 28, 2016).

Framework and thus decreases the comparability of FCA's capital requirements to those of the U.S. Rule.

The System Comment Letter and AgriBank, FCB (AgriBank), also requested that we consider changes to the definition of UREE in § 628.2 if we retain the URE requirement.

Under the existing definition, nonqualified allocated equities not subject to redemption or revolvment are included in the definition of UREE and count towards an institution's minimum URE and UREE requirement, provided that certain additional stipulations are met.⁵⁸ Such equities allocated to other System institutions are expressly excluded. The commenters assert that, because of the deductions and eliminations for computing regulatory capital under FCA's 2017 Capital Rule, equities allocated by a System bank to an association satisfy the objectives for URE and UREE as previously outlined by FCA.⁵⁹

The request to reconsider application of the minimum URE and UREE requirements or to change the

⁵⁸ To include nonqualified allocated equities in UREE, an institution's board must designate the equities as UREE at issuance and undertake in its capitalization bylaws or a board resolution 1.) not to change the designation without FCA prior approval, 2.) not to exercise discretion to revolve the equities except under dissolution or liquidation, and 3.) not offset the equities against a loan in default except as required by a court of competent jurisdiction, or if required under § 615.5290 in connection with a restructuring.

⁵⁹ URE and UREE provide a cushion from losses for both third-party and common cooperative equities and protect against interconnected risk between System banks and associations. See 79 FR 52814 (September 4, 2014).

definition of UREE is beyond the scope of the proposal. We explained at length our position on the significance of URE and UREE to System capitalization in the preamble to the 2017 Capital Rule.⁶⁰

We note that the System Comment Letter and AgriBank drew a connection between our interpretation that allocated equities are “paid-in”, as defined by Basel, and their argument for the elimination of the URE and UREE requirements. The interpretation that allocated equities meet the Basel definition of paid-in capital, as discussed in the proposal,⁶¹ does not diminish the importance of the URE and UREE requirements.⁶²

The minimum URE and UREE requirement as presently calculated protects association members against association losses, associations against bank losses, and the System against financial contagion. Financial contagion in this context would include impacts to earnings measures that are relevant to System investors and FCA’s evaluations of the safety and soundness of

⁶⁰ See 81 FR 49720, 49732-49735 (July 28, 2016).

⁶¹ See 81 FR 55786, 55791 (September 10, 2020).

⁶² As noted in the System Comment Letter, Basel III recognizes two broad categories of CET1 capital: retained earnings and paid-in capital instruments. Consistent with that view, our capital rules acknowledge and draw distinction between these two types of CET1 capital (§ 628.20(b)(1) and (2)). Our interpretation that common cooperative equities are “paid-in” as defined by Basel does not eliminate the distinction between these two types of high-quality capital. Equities allocated by one System institution to another are at risk at both institutions and present a risk of financial contagion as a result of the interconnection that gives rise to their existence. Unallocated retained earnings and equivalents (as presently defined) do not present the same contagion risk.

System institutions. In addition to our previously stated position, we note that URE at a System bank ensures the bank can act as a source of strength and provide assistance to district associations or other banks if needed, and it also insulates a bank's affiliated associations from losses in other districts in the event of a joint and several liability call.

F. Service Corporation Deductions and Adjustments

Existing § 628.22(a)(6) requires a System institution to deduct any allocated equity investment in another System institution. We proposed to expand the deduction requirement to include allocated equity investments in a System service corporation.⁶³ The System Comment Letter indicated that System institutions are unaware of any service corporations that allocate equities and provided no further comment on the amendment proposed. Accordingly, we are adopting the revision as proposed.

As we noted in the preamble to the proposed rule, in November 2016 the Farm Credit Council sent a letter⁶⁴ to FCA requesting that institutions be permitted to

⁶³ System institution is defined in existing § 628.2 as "a System bank, an association of the Farm Credit System,... and any other institution chartered by the FCA that the FCA determines should be considered a System institution for the purposes of this part." The FCA has not made any determinations to include other institutions in this definition.

⁶⁴ Letter dated November 22, 2016, from Charles Dana, General Counsel, Farm Credit Council to Gary K. Van Meter, Director, Office of Regulatory Policy. This letter was received after the 2017 Capital Rule had been adopted by the FCA Board and communicated a request to change certain provisions of the 2017 Capital Rule, as discussed in this section.

risk-weight their investments in System service corporations at 100 percent instead of having to deduct the investments from CET1 capital in their regulatory capital calculations. The Farm Credit Council further requested FCA to establish regulatory capital treatments for unincorporated business entities (UBEs) based on the specific nature of the entity in question. We responded to this request in the preamble to the proposed rule, declining to revise the requirement to deduct equity investments in service corporations from regulatory capital and noting that we retain the authority to consider the appropriate capital treatment of UBEs on a case-by-case basis.

The System Comment Letter requested that we reconsider our position on service corporation investments. The System believes the requirement to deduct investments in System service corporations is inconsistent with the level of risk in the investments and state that the deduction requirement discourages the formation of organizations that provide an efficient means for cooperation among System institutions in providing services to their stockholders. The System further noted that all service corporations are subject to chartering requirements and that FCA can establish the individual

capital requirements of a service corporation on a case-by-case basis.

We are not convinced of the need to change our previously communicated position. As we stated in the preamble to the proposed rule, we believe that investments in service corporations are committed to support the risks at the service corporation and must be available to meet the service corporation's capital needs.⁶⁵ This position and our resulting regulatory capital treatment of investments in service corporations are consistent with our treatment of all intra-System investments. The System accurately points out that FCA can establish individual capital requirements for service corporations as part of the chartering process. We believe the more prudent default treatment is deduction rather than risk weighting. We would consider risk weighting on a case-by-case basis as the exception.

G. Adjustments for Accruing Patronage and Dividends

We proposed to amend the regulatory capital adjustment and deduction requirements under § 628.22 by incorporating in proposed § 628.22(b) the existing call report instructions directing System institutions to reverse the accrual of patronage or dividend payables or receivables that occur prior to a board declaration

⁶⁵ See 85 FR 55786, 55795 (September 10, 2020).

resolution.⁶⁶ As discussed in the proposed rule preamble, FCA believes it is important to reflect regulatory capital on the basis of related contractual obligations. Some options for the treatment of patronage and dividend accruals under GAAP may not be consistent with this regulatory capital requirement.⁶⁷ FCA looks to the date an institution's board of directors passes a binding resolution declaring an amount it will pay in patronage or dividends⁶⁸ to establish when the legal obligation exists and should be reflected in regulatory capital computations. We received no comments on this amendment and are adopting it as proposed.

H. Bank Disclosures

We proposed clarifying amendments to the requirement under § 628.63(b)(4) that banks disclose a reconciliation of their regulatory capital elements to their balance sheets in any audited consolidated financial statements. Specifically, we proposed to add the word "applicable" before "audited" to clarify that reconciliation requirements apply only to current period financial statements that have been audited.⁶⁹ We further proposed that System banks be required to

⁶⁶ See existing Call Report instructions for Schedule RC-R.4, Line item 3 at <https://www.fca.gov/bank-oversight/fcs-call-reports>.

⁶⁷ See 85 FR 55786, 55787-55788 (September 10, 2020).

⁶⁸ The declaration must include an amount to be paid or include language by which an amount could be calculated.

⁶⁹ Under FCA regulations, only the annual report to shareholders prepared at yearend must be audited. See § 620.5(j)(1).

complete this reconciliation of regulatory capital elements using both point-in-time and three-month average daily balance regulatory capital values as our regulatory capital requirements are based on a three-month average daily balance.⁷⁰ Financial statements are generally prepared using point-in-time information.

The System Comment Letter questioned the value added by completing the required reconciliation on both a point-in-time and a three-month average daily balance basis. The commenters noted that Basel III Pillar 3 disclosure requirements are based on a tieback to audited financial statements, which are prepared on a point-in-time basis. They further noted that the addition of the three-month average reconciliation was unnecessary and potentially confusing.

We are persuaded that completing the reconciliation on a point-in-time basis satisfies the Basel III Pillar 3 disclosure requirement for a reconciliation of regulatory capital to GAAP capital. We acknowledge that requiring a reconciliation on two separate bases would have added another administrative requirement. We have decided instead to revise § 628.63(b)(4) to require only a reconciliation on a point-in-time basis, together with a statement that compliance with the minimum capital requirements in

⁷⁰ See § 628.10(a).

subpart B of part 628 is determined using average daily balances for the most recent 3 months.

To address potential conflicts between the requirements of §§ 620.3 and 628.62(c), we proposed to revise § 620.3 to state that, unless otherwise determined by FCA, the use of the authorized limited disclosure in § 628.62(c) does not create an incomplete disclosure. We also proposed to revise § 620.3 to permit institutions to modify the required statement that the information provided is true, accurate, and complete to explain that the completeness of the disclosure was determined in consideration of § 628.62(c). We received no comments on this amendment and are adopting it as proposed.

Lastly, we proposed to remove and reserve § 628.63(b)(3), which required disclosure of the computation of regulatory capital ratios during the transition period, because the provision is no longer applicable. We received no comments on this amendment and are adopting it as proposed.

I. Retirement of Statutory Borrower Stock

Under existing § 628.20(b)(1)(xiv)(B), System institutions may redeem the minimum statutory borrower stock described in § 628.20(b)(1)(x) without prior FCA approval and without satisfying the minimum holding period for common cooperative equities included in CET1

capital. In order to eliminate any possible misinterpretation that an institution could retire statutory borrower stock if the institution were not meeting its regulatory capital requirements, we proposed to add a provision to § 628.20(b)(1)(xiv)(B) to clarify that institutions may redeem statutory borrower stock only provided that, after such redemption, the institution continues to comply with all minimum regulatory capital requirements.

The System Comment Letter and Compeer requested that we reconsider the regulatory provisions for redemptions of statutory minimum borrower stock because of the administrative burden they create for small-balance loans at some institutions (those with balances of \$50,000 or less). As we clarified in the preamble to the proposed rule, under the existing provisions of § 628.20(b)(1)(xiv)(B), for any statutory borrower stock exceeding \$1,000 or 2 percent of the loan amount, *whichever is less*, the minimum holding periods for inclusion in regulatory capital apply.⁷¹ We also clarified in the preamble that the 2 percent of the loan amount is determined relative to the originated loan amount. Commenters stated that, under this structure, some System institutions must undertake a

⁷¹ See 85 FR 55786, 55794 (September 10, 2020). Of note, under § 628.20(b)(1)(x) and (d)(1)(viii), any statutory borrower stock in excess of the statutory minimum that is funded through loan proceeds from the System institution is includable only in tier 2 capital.

"burdensome process" to track the holding period for stock that is \$1,000 or less but greater than 2 percent of the loan balance. The commenters further noted that the amounts of capital retained as a result of this requirement are de minimis in terms of any institution's total capital.

We are persuaded that the burden of tracking and managing these de minimis amounts of statutory minimum borrower stock in accordance with existing requirements is not justified by the safety and soundness benefits of the nominal amounts of capital retained. Accordingly, we are amending the provisions of § 628.20(b)(1)(xiv)(B) to reflect that an amount of the statutory borrower stock as described in section 4.3A of the Act, not to exceed \$1,000, may be redeemed without a minimum period outstanding after issuance and without the prior approval of the FCA. This amendment eliminates the burden of tracking de minimis amounts of statutory borrower stock that are less than \$1,000 but exceed 2 percent of the loan balance. More specifically, System institutions may redeem up to \$1,000 of statutory borrower stock irrespective of the proportional relationship of the stock investment and the originated loan amount. We are making conforming changes to § 628.20(b)(1)(x) and (d)(1)(viii)(C) to incorporate this change.

The ABA commented that it appreciated our clarification but asserted that the proposal would still leave FCS institutions subject to very lax requirements concerning stock redemptions compared to those applicable to commercial banks. We note that the proposed amendment eliciting this comment does not reduce restrictions on stock redemptions for System institutions. As discussed in the preamble to the proposed rule, the proposed amendment is merely a technical clarification for the avoidance of doubt.⁷²

As stated in the preamble to the 2017 Capital Rule, one of our objectives was to ensure the System's capital requirements are comparable to the Basel III framework and the standardized approach under the U.S. Rule, taking into consideration the cooperative structure and the organization of the System.⁷³ Accordingly, while most requirements of our rule are similar or identical to requirements in the U.S. Rule, the cooperative structure and the organization of System institutions necessitated modification of other requirements. A piecemeal comparison of various elements of the two rules will not yield an accurate appraisal of the regulatory outcome of our requirements as compared to the U.S. Rule.

⁷² 85 FR 55786, 55794 (September 10, 2020).

⁷³ See objectives in 81 FR 49720 (July 28, 2016).

As the ABA points out, when restrictions on stock redemptions are considered in isolation of other rule requirements, commercial banks are subject to more restrictions than System institutions. For example, to retire stock, national banks must obtain the approval of shareholders owning two thirds of the shares in each affected class, as well as prior approval from the OCC.⁷⁴ By contrast, System institutions may redeem common cooperative equities without obtaining FCA or shareholder prior approval, provided certain conditions are met.⁷⁵ We acknowledged and discussed this difference in the preamble to the 2017 Capital Rule.⁷⁶ However, the requirements for stock redemptions should not be evaluated in isolation of the remaining restrictions on distributions in FCA's capital rules.

First, FCA's Safe Harbor for stock redemptions applies only to common cooperative equities; all other capital instruments including preferred stock and subordinated debt cannot be redeemed or retired prior to their maturity without express prior approval from

⁷⁴ 12 U.S.C. 59.

⁷⁵ Under § 628.20(f)(5), institutions may retire common cooperative equities included in CET1 capital a minimum of 7 years after the issuance date, and they may retire common cooperative equities included in tier 2 capital a minimum of 5 years after the issuance date. In the case of common cooperative equities included in CET1, after such retirements the dollar amount of CET1 capital outstanding must equal or exceed the dollar amount outstanding one year earlier. Under § 628.20(b)(1)(xiv)(B), statutory minimum borrower stock may be retired without a minimum period outstanding after issuance and without the prior approval of FCA.

⁷⁶ See 81 FR 49720, 49731 (July 28, 2016).

the FCA Board.⁷⁷ Second, the most flexible treatment of stock redemptions under FCA's existing capital rules, which is the focus of the ABA's comments, is applicable only to minimum statutory borrower stock.⁷⁸ This capital element comprises less than 1 percent of the System's total capital base.⁷⁹ All other common cooperative equities included in regulatory capital are subject to further restrictions including minimum holding periods before they can be redeemed without obtaining prior approval from FCA.⁸⁰ A third consideration is that a significant portion of allocated equities in the System has been designated as unallocated retained earnings equivalents,⁸¹ a type of common cooperative equity that cannot be redeemed without obtaining prior approval from the FCA Board.⁸²

⁷⁷ See § 628.20(c)(1)(vi) and (d)(1)(X).

⁷⁸ Statutory minimum borrower stock is stock acquired by System borrowers to satisfy requirements under Section 4.3A of the Act. It is equal to the lesser of \$1,000 or 2 percent of the loan.

⁷⁹ As of June 30, 2021, System entities reported combined total regulatory capital of \$65.8 billion, of which \$0.39 billion or 0.6 percent was comprised of statutory minimum borrower stock that is already eligible to be redeemed without a minimum holding period under existing regulatory requirements. This rulemaking does not change the requirements governing redemption of this stock.

⁸⁰ See § 628.20(f)(5).

⁸¹ As defined in § 628.2, unallocated retained earnings (URE) equivalents include nonqualified allocated equities designated as URE equivalents at issuance that a System institution undertakes not to revolve except upon dissolution or liquidation. Under new § 628.21, System institutions are required to obtain prior FCA approval before re-designating URE equivalents as equities that the institution has discretion to redeem.

⁸² As of March 31, 2021, System entities reported a combined total regulatory capital of \$65.8 billion, of which \$19.2 billion (29 percent) was comprised of allocated common cooperative equities. Of the \$19.1 billion in allocated common cooperative equities, \$11.9 billion (62 percent) were designated as unallocated retained earnings equivalents.

Finally and most importantly, as previously discussed in the preamble to the 2017 Capital Rule, the redemptions we allow must be considered in the context of our overall limitations on capital distributions.⁸³ Under the provisions of FCA's Safe Harbor Deemed Prior Approval,⁸⁴ all capital distributions by a System institution, including redemptions of common cooperative equities, dividends, and cash patronage, are limited to no more than the year-over-year dollar increase in CET1 capital for any given 12-month period. All other factors held constant, this in effect limits System institutions to distributing no more than the current year's net income. By contrast, national banks have statutory authority to distribute cash dividends in amounts up to current year's net income plus the retained net income for the two previous years.⁸⁵ As we noted in the preamble to the 2017 Capital Rule, we believe that our Safe Harbor for equities is appropriately comparable to Basel III and the U.S. Rule because the Safe Harbor's broader application to total cash dividend payments, cash patronage payments, and equity redemptions or revolvments is tempered by an overall limit that is more restrictive than commercial banks' safe harbor to pay cash dividends.⁸⁶

⁸³ See 81 FR 49720, 49731 (July 28, 2016).

⁸⁴ § 628.20(f)(5).

⁸⁵ 12 U.S.C. 60.

⁸⁶ See 81 FR 49720, 49731 (July 28, 2016).

IV. Abbreviations

BCBS	Basel Committee on Banking Supervision
CFR	Code of Federal Regulations
CFTC	Commodity Futures Trading Commission
EMNA	Eligible Master Netting Agreement
FCA	Farm Credit Administration
FDIC	Federal Deposit Insurance Corporation
FDI Act	Federal Deposit Insurance Corporation Improvement Act of 1991
FFIEC	Federal Financial Institutions Examination Council
FR	Federal Register
FRB	Board of Governors of the Federal Reserve System
GAAP	Generally Accepted Accounting Principles (U.S.)
GSE	Government-Sponsored Enterprise
GSIB	Global Systemically Important Bank
OCC	Office of the Comptroller of the Currency
QFC	Qualified Financial Contract
QMNA	Qualified Master Netting Agreement
SEC	Securities and Exchange Commission
SFA	Supervisory Formula Approach
SRWA	Simple Risk-Weight Approach
SSFA	Simplified Supervisory Formula Approach
UBE	Unincorporated Business Entity
URE	Unallocated Retained Earnings
UREE	Unallocated Retained Earnings Equivalents
U.S.C.	United States Code

V. Regulatory Analysis

A. Regulatory Flexibility Act

Pursuant to section 605(b) of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.), FCA hereby certifies that this final rule will not have a significant economic impact on a substantial number of small entities. Each of the banks in the System, considered together with its affiliated associations, has assets and annual income in excess of the amounts that would qualify them as small entities. Therefore,

System institutions are not "small entities" as defined in the Regulatory Flexibility Act.

B. Congressional Review Act

Under the provisions of the Congressional Review Act (5 U.S.C. 801 et seq.), the Office of Management and Budget's Office of Information and Regulatory Affairs has determined that this final rule is not a "major rule" as the term is defined at 5 U.S.C. 804(2).

List of Subjects

12 CFR Part 614

Agriculture, Banks, Banking, Foreign trade, Reporting and recordkeeping requirements, Rural areas.

12 CFR Part 615

Accounting, Agriculture, Banks, Banking, Government securities, Investments, Rural areas.

12 CFR Part 620

Accounting, Agriculture, Banks, Banking, Reporting and recordkeeping requirements, Rural areas.

12 CFR Part 628

Accounting, Agriculture, Banks, Banking, Capital, Government securities, Investments, Rural areas.

For the reasons stated in the preamble, the Farm Credit Administration amends parts 614, 615, 620, and 628 of chapter VI, title 12 of the Code of Federal Regulations as follows:

PART 614--LOAN POLICIES AND OPERATIONS

1. The authority citation for part 614 is revised to read as follows:

Authority: secs. 1.3, 1.5, 1.6, 1.7, 1.9, 1.10, 1.11, 2.0, 2.2, 2.3, 2.4, 2.10, 2.12, 2.13, 2.15, 3.0, 3.1, 3.3, 3.7, 3.8, 3.10, 3.20, 3.28, 4.12, 4.12A, 4.13B, 4.14, 4.14A, 4.14D, 4.14E, 4.18, 4.18A, 4.19, 4.25, 4.26, 4.27, 4.28, 4.36, 4.37, 5.9, 5.10, 5.17, 7.0, 7.2, 7.6, 7.8, 7.12, 7.13, 8.0, 8.5 of the Farm Credit Act (12 U.S.C. 2011, 2013, 2014, 2015, 2017, 2018, 2019, 2071, 2073, 2074, 2075, 2091, 2093, 2094, 2097, 2121, 2122, 2124, 2128, 2129, 2131, 2141, 2149, 2183, 2184, 2201, 2202, 2202a, 2202d, 2202e, 2206, 2206a, 2207, 2211, 2212, 2213, 2214, 2219a, 2219b, 2243, 2244, 2252, 2279a, 2279a-2, 2279b, 2279c-1, 2279f, 2279f-1, 2279aa, 2279aa-5); 12 U.S.C. 2121 note; 42 U.S.C. 4012a, 4104a, 4104b, 4106, and 4128.

2. Amend § 614.4351 by revising paragraph (a) to read as follows:

§ 614.4351 Computation of lending and leasing limit base.

(a) *Lending and leasing limit base.* An institution's lending and leasing limit base is composed of the total capital (tier 1 and tier 2) of the institution, as defined in § 628.2 of this chapter, with adjustments applicable to the institution provided

for in § 628.22 of this chapter, and with the following further adjustments:

(1) [Reserved]

(2) Eligible third-party capital that is required to be excluded from total capital under § 628.23 of this chapter may be included in the lending limit base.

* * * * *

PART 615—FUNDING AND FISCAL AFFAIRS, LOAN POLICIES AND OPERATIONS, AND FUNDING OPERATIONS

3. The authority citation for part 615 is revised to read as follows:

Authority: Secs. 1.5, 1.7, 1.10, 1.11, 1.12, 2.2, 2.3, 2.4, 2.5, 2.12, 3.1, 3.7, 3.11, 3.25, 4.3, 4.3A, 4.9, 4.14B, 4.25, 5.9, 5.17, 8.0, 8.3, 8.4, 8.6, 8.8, 8.10, 8.12 of the Farm Credit Act (12 U.S.C. 2013, 2015, 2018, 2019, 2020, 2073, 2074, 2075, 2076, 2093, 2122, 2128, 2132, 2146, 2154, 2154a, 2160, 2202b, 2211, 2243, 2252, 2279aa, 2279aa-3, 2279aa-4, 2279aa-6, 2279aa-8, 2279aa-10, 2279aa-12); 12 U.S.C. 2154 note; 15 U.S.C. 78o-7 note.

4. Revise § 615.5200 to read as follows:

§ 615.5200 Capital planning.

(a) The Board of Directors of each System institution shall determine the amount of regulatory capital needed to assure the System institution's continued financial viability and to provide for growth

necessary to meet the needs of its borrowers. The minimum capital standards specified in this part and part 628 of this chapter are not meant to be adopted as the optimal capital level in the System institution's capital adequacy plan. Rather, the standards are intended to serve as minimum levels of capital that each System institution must maintain to protect against the credit and other general risks inherent in its operations.

(b) Each Board of Directors shall establish, adopt, and maintain a formal written capital adequacy plan as a part of the financial plan required by § 618.8440 of this chapter. The plan shall include the capital targets that are necessary to achieve the System institution's capital adequacy goals as well as the minimum permanent capital, common equity tier 1 (CET1) capital, tier 1 capital, total capital, and tier 1 leverage ratios (including the unallocated retained earnings (URE) and URE equivalents minimum) standards. The plan shall expressly acknowledge the continuing and binding effect of all board resolutions adopted in accordance with § 628.20(b)(1)(xiv), (c)(1)(xiv), and (d)(1)(xi) of this chapter, and with § 628.21 of this chapter. The plan shall address any projected dividend payments, patronage payments, equity retirements, or other action that may decrease the System institution's

capital or the components thereof for which minimum amounts are required by this part and part 628 of this chapter. The plan shall set forth the circumstances and minimum timeframes in which equities may be redeemed or revolved consistent with the System institution's applicable bylaws or board of directors' resolutions.

(c) In addition to factors that must be considered in meeting the minimum standards, the board of directors shall also consider at least the following factors in developing the capital adequacy plan:

(1) Capability of management and the board of directors (the assessment of which may be a part of the assessments required in paragraphs (b)(2)(ii) and (b)(7)(i) of § 618.8440 of this chapter);

(2) Quality of operating policies, procedures, and internal controls;

(3) Quality and quantity of earnings;

(4) Asset quality and the adequacy of the allowance for losses to absorb potential loss within the loan and lease portfolios;

(5) Sufficiency of liquid funds;

(6) Needs of a System institution's customer base; and

(7) Any other risk-oriented activities, such as funding and interest rate risks, potential obligations under joint and several liability, contingent and off-

balance-sheet liabilities or other conditions warranting additional capital.

5. Amend § 615.5201 by revising the definition of "System institution" to read as follows:

§ 615.5201 Definitions.

* * * * *

System institution means a System bank, an association of the Farm Credit System, and their successors, and any other institution chartered by the Farm Credit Administration (FCA) that the FCA determines should be considered a System institution for the purposes of this subpart.

* * * * *

6. Amend § 615.5220 by revising paragraph (a) (6) to read as follows:

§ 615.5220 Capitalization bylaws.

(a) * * *

(6) The manner in which equities will be retired, including a provision stating that equities other than those protected under section 4.9A of the Act are retireable at the sole discretion of the board, provided minimum capital adequacy standards established by the Farm Credit Administration, and the capital requirements established by the board of directors of the System institution, are met;

* * * * *

PART 620—DISCLOSURE TO SHAREHOLDERS

7. The authority citation for part 620 continues to read as follows:

Authority: Secs. 4.3, 4.3A, 4.19, 5.9, 5.17, 5.19 of the Farm Credit Act (12 U.S.C. 2154, 2154a, 2207, 2243, 2252, 2254); sec. 424 of Pub. L. 100-233, 101 Stat. 1568, 1656; sec. 514 of Pub. L. 102-552, 106 Stat. 4102.

8. Amend § 620.3 by adding a sentence at the ends of paragraphs (a) and (c) (3) to read as follows:

§ 620.3 Accuracy of reports and assessment of internal control over financial reporting.

(a) * * * Unless otherwise determined by the Farm Credit Administration (FCA), the appropriate use of the limited disclosure authorized by § 628.62(c) of this chapter does not create an incomplete disclosure.

* * * * *

(c) * * *

(3) * * * If the report contains the limited disclosure authorized by § 628.62(c) of this chapter, the statement may be modified to explain that the completeness of the report was determined in consideration of § 628.62(c).

* * * * *

9. Amend § 620.5 by adding paragraph (f)(3)(v) and revising paragraph (f)(4) to read as follows:

§ 620.5 Contents of the annual report to shareholders.

* * * * *

(f) * * *

(3) * * *

(v) Tier 1 leverage ratio.

(4) *For all banks (on a bank only basis) and for all associations.* The following ratios shall be disclosed in comparative columnar form in each annual report through fiscal year end 2021, only as long as these ratios are part of the previous 5 fiscal years of financial data required under paragraphs (f)(2) and (3) of this section:

(i) Core surplus ratio.

(ii) Total surplus ratio.

(iii) For banks only, net collateral ratio.

* * * * *

PART 628—CAPITAL ADEQUACY OF SYSTEM INSTITUTIONS

10. The authority citation for part 628 is revised to read as follows:

Authority: Secs. 1.5, 1.7, 1.10, 1.11, 1.12, 2.2, 2.3, 2.4, 2.5, 2.12, 3.1, 3.7, 3.11, 3.25, 4.3, 4.3A, 4.9, 4.14B, 4.25, 5.9, 5.17, 8.0, 8.3, 8.4, 8.6, 8.8, 8.10, 8.12 of the Farm Credit Act (12 U.S.C. 2013, 2015, 2018, 2019, 2020, 2073, 2074, 2075, 2076, 2093,

2122, 2128, 2132, 2146, 2154, 2154a, 2160, 2202b, 2211, 2243, 2252, 2279aa, 2279aa-3, 2279aa-4, 2279aa-6, 2279aa-8, 2279aa-10, 2279aa-12); 12 U.S.C. 2154 note; 15 U.S.C. 78o-7 note.

11. Amend § 628.2 by:

- a. Revising the definition of "Collateral agreement";
- b. Adding in alphabetical order a definition for "Common cooperative equity issuance date"; and
- c. Revising the definitions of "Eligible margin loan", "Qualifying master netting agreement", "Repo-style transaction", and "System institution".

The revisions and addition read as follows:

§ 628.2 Definitions.

* * * * *

Collateral agreement means a legal contract that specifies the time when, and circumstances under which, a counterparty is required to pledge collateral to a System institution for a single financial contract or for all financial contracts in a netting set and confers upon the System institution a perfected, first-priority security interest (notwithstanding the prior security interest of any custodial agent), or the legal equivalent thereof, in the collateral posted by the counterparty under the agreement. This security

interest must provide the System institution with a right to close-out the financial positions and liquidate the collateral upon an event of default of, or failure to perform by, the counterparty under the collateral agreement. A contract would not satisfy this requirement if the System institution's exercise of rights under the agreement may be stayed or avoided:

(1) Under applicable law in the relevant jurisdictions, other than:

(i) In receivership, conservatorship, or resolution under the Federal Deposit Insurance Act, Title II of the Dodd-Frank Act, or under any similar insolvency law applicable to Government-sponsored enterprises (GSEs), or laws of foreign jurisdictions that are substantially similar to the U.S. laws referenced in this paragraph (1)(i) in order to facilitate the orderly resolution of the defaulting counterparty;

(ii) Where the agreement is subject by its terms to, or incorporates, any of the laws referenced in paragraph (1)(i) of this definition; or

(2) Other than to the extent necessary for the counterparty to comply with the requirements of part 47, subpart I of part 252, or part 382 of this title, as applicable.

* * * * *

Common cooperative equity issuance date means the date in which the holding period for purchased stock (excluding statutory minimum borrower stock and third-party stock) and allocated equities start:

(1) For allocated equities, the calendar quarter-ending in which:

(i) The System institution's Board of Directors has passed a resolution declaring a patronage refund; and

(ii) The System institution has completed the applicable accounting treatment by segregating the new allocated equities from its unallocated retained earnings.

(2) For purchased stock (excluding statutory minimum borrower stock and third-party stock), the calendar quarter-ending in which the stock is acquired by the holder and recognized on the institution's balance sheet.

* * * * *

Eligible margin loan means:

(1) An extension of credit where:

(i) The extension of credit is collateralized exclusively by liquid and readily marketable debt or equity securities, or gold;

(ii) The collateral is marked-to-fair value daily, and the transaction is subject to daily margin maintenance requirements; and

(iii) The extension of credit is conducted under an agreement that provides the System institution the right to accelerate and terminate the extension of credit and to liquidate or set-off collateral promptly upon an event of default, including upon an event of receivership, insolvency, liquidation, conservatorship, or similar proceeding, of the counterparty, provided that, in any such case:

(A) Any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions, other than:

(1) In receivership, conservatorship, or resolution under the Federal Deposit Insurance Act, Title II of the Dodd-Frank Act, or under any similar insolvency law applicable to GSEs,² or laws of foreign jurisdictions that are substantially similar to the U.S. laws referenced in this paragraph (1)(iii)(A)(1) in order to

² This requirement is met where all transactions under the agreement are (i) executed under U.S. law and (ii) constitute "securities contracts" under section 555 of the Bankruptcy Code (11 U.S.C. 555), qualified financial contracts under section 11(e)(8) of the Federal Deposit Insurance Act, or netting contracts between or among financial institutions under sections 401-407 of the Federal Deposit Insurance Corporation Improvement Act or the Federal Reserve Board's Regulation EE (12 CFR part 231).

facilitate the orderly resolution of the defaulting counterparty; or

(2) Where the agreement is subject by its terms to, or incorporates, any of the laws referenced in paragraph (1)(iii)(A)(1) of this definition; and

(B) The agreement may limit the right to accelerate, terminate, and close-out on a net basis all transactions under the agreement and to liquidate or set-off collateral promptly upon an event of default of the counterparty to the extent necessary for the counterparty to comply with the requirements of part 47, subpart I of part 252, or part 382 of this title, as applicable.

(2) In order to recognize an exposure as an eligible margin loan for purposes of this subpart, a System institution must comply with the requirements of § 628.3(b) with respect to that exposure.

* * * * *

Qualifying master netting agreement means a written, legally enforceable agreement provided that:

(1) The agreement creates a single legal obligation for all individual transactions covered by the agreement upon an event of

default following any stay permitted by paragraph (2) of this definition, including upon an event of receivership, conservatorship, insolvency, liquidation, or similar proceeding, of the counterparty;

(2) The agreement provides the System institution the right to accelerate, terminate, and close-out on a net basis all transactions under the agreement and to liquidate or set-off collateral promptly upon an event of default, including upon an event of receivership, conservatorship, insolvency, liquidation, or similar proceeding, of the counterparty, provided that, in any such case:

(i) Any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions, other than:

(A) In receivership, conservatorship, or resolution under the Federal Deposit Insurance Act, Title II of the Dodd-Frank Act, or under any similar insolvency law applicable to GSEs, or laws of foreign jurisdictions that are substantially similar to the U.S. laws referenced in this paragraph (2) (i) (A) in order

to facilitate the orderly resolution of the defaulting counterparty; or

(B) Where the agreement is subject by its terms to, or incorporates, any of the laws referenced in paragraph (2)(i)(A) of this definition; and

(ii) The agreement may limit the right to accelerate, terminate, and close-out on a net basis all transactions under the agreement and to liquidate or set-off collateral promptly upon an event of default of the counterparty to the extent necessary for the counterparty to comply with the requirements of part 47, subpart I of part 252, or part 382 of this title, as applicable;

(3) The agreement does not contain a walkaway clause (that is, a provision that permits a non-defaulting counterparty to make a lower payment than it otherwise would make under the agreement, or no payment at all, to a defaulter or the estate of a defaulter, even if the defaulter or the estate of the defaulter is a net creditor under the agreement); and

(4) In order to recognize an agreement as a qualifying master netting agreement for purposes of this subpart, a System institution must

comply with the requirements of § 628.3(d) with respect to that agreement.

Repo-style transaction means a repurchase or reverse repurchase transaction, or a securities borrowing or securities lending transaction, including a transaction in which the System institution acts as agent for a customer and indemnifies the customer against loss, provided that:

(1) The transaction is based solely on liquid and readily marketable securities, cash, or gold;

(2) The transaction is marked-to-fair value daily and subject to daily margin maintenance requirements;

(3) (i) The transaction is a "securities contract" or "repurchase agreement" under section 555 or 559, respectively, of the Bankruptcy Code (11 U.S.C. 555 or 559), a qualified financial contract under section 11(e)(8) of the Federal Deposit Insurance Act, or a netting contract between or among financial institutions under sections 401 - 407 of the Federal Deposit Insurance Corporation Improvement Act or the Federal Reserve's Regulation EE (12 CFR part 231); or

(ii) If the transaction does not meet the criteria set forth in paragraph (3)(i) of this definition, then either:

(A) The transaction is executed under an agreement that provides the System institution the right to accelerate, terminate, and close-out the transaction on a net basis and to liquidate or set-off collateral promptly upon an event of default, including upon an event of receivership, insolvency, liquidation, or similar proceeding, of the counterparty, provided that, in any such case:

(1) Any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions, other than:

(i) In receivership, conservatorship, or resolution under the Federal Deposit Insurance Act, Title II of the Dodd-Frank Act, or under any similar insolvency law applicable to GSEs, or laws of foreign jurisdictions that are substantially similar to the U.S. laws referenced in this paragraph (3)(ii)(A)(1)(i) in order to facilitate the orderly resolution of the defaulting counterparty;

(ii) Where the agreement is subject by its terms to, or incorporates, any of the laws referenced in paragraph (3)(ii)(A)(1)(i) of this definition; and

(2) The agreement may limit the right to accelerate, terminate, and close-out on a net basis all transactions under the agreement and to liquidate or set-off collateral promptly upon an event of default of the counterparty to the extent necessary for the counterparty to comply with the requirements of part 47, subpart I of part 252, or part 382 of this title, as applicable; or

(B) The transaction is:

(1) Either overnight or unconditionally cancelable at any time by the System institution; and

(2) Executed under an agreement that provides the System institution the right to accelerate, terminate, and close-out the transaction on a net basis and to liquidate or set-off collateral promptly upon an event of counterparty default; and

(4) In order to recognize an exposure as a repo-style transaction for purposes of this subpart, a System institution must comply with

the requirements of § 628.3(e) with respect to that exposure.

* * * * *

System institution means a System bank, an association of the Farm Credit System, and their successors, and any other institution chartered by the Farm Credit Administration (FCA) that the FCA determines should be considered a System institution for the purposes of this subpart.

* * * * *

12. Amend § 628.10 by revising paragraph (c)(4) to read as follows:

§ 628.10 Minimum capital requirements.

* * * * *

(c) * * *

(4) *Tier 1 leverage ratio.* (i) A System institution's leverage ratio is the ratio of the institution's tier 1 capital to the institution's average total consolidated assets as reported on the institution's Call Report net of deductions and adjustments from tier 1 capital under §§ 628.22(a), (b), and (c) and 628.23.

(ii) To calculate the measure of URE and URE equivalents described in paragraph (b)(4) of this section, a System institution must adjust

URE and URE equivalents to reflect all the deductions and adjustments required under § 628.22(a), (b), and (c), and must use the denominator of the tier 1 leverage ratio.

* * * * *

13. Amend § 628.20 by revising paragraphs (b)(1)(i), (ii), (x), and (xiv), (c)(1)(xiv), (d)(1)(i), (d)(1)(viii)(C), (d)(1)(xi), and (f)(5)(ii) to read as follows:

§ 628.20 Capital components and eligibility criteria for tier 1 and tier 2 capital instruments.

* * * * *

(b) * * *

(1) * * *

(i) The instrument is paid-in, issued directly by the System institution, and represents the most subordinated claim in a receivership, insolvency, liquidation, or similar proceeding of the System institution;

(ii) The holder of the instrument is entitled to a claim on the residual assets of the System institution after all senior claims have been satisfied in a receivership, insolvency, liquidation, or similar proceeding;

* * * * *

(x) The System institution, or an entity that the System institution controls, did not purchase or directly or indirectly fund the purchase of the

instrument, except that where there is an obligation for a member of the institution to hold an instrument in order to receive a loan or service from the System institution, an amount of that loan equal to no more than \$1,000 of the borrower stock requirement under section 4.3A of the Act will not be considered as a direct or indirect funding where:

(A) The purpose of the loan is not the purchase of capital instruments of the System institution providing the loan; and

(B) The purchase or acquisition of one or more member equities of the institution is necessary in order for the beneficiary of the loan to become a member of the System institution;

* * * * *

(xiv) The System institution's capitalization bylaws, or a resolution adopted by its board of directors under § 628.21, provides that the institution:

(A) Establishes a minimum redemption or revolvment period of 7 years for equities included in CET1; and

(B) Shall not redeem, revolve, cancel, or remove any equities included in CET1 without prior approval of the FCA under paragraph (f) of this section, except that the statutory borrower stock

described in paragraph (b) (1) (x) of this section, not to exceed \$1,000, may be redeemed without a minimum period outstanding after issuance and without the prior approval of the FCA, as long as after the redemption, the System institution continues to comply with all minimum regulatory capital requirements.

* * * * *

(c) * * *

(1) * * *

(xiv) The System institution's capitalization bylaws, or a resolution adopted by its board of directors under § 628.21, provides that the institution:

(A) Establishes a minimum redemption or no-call period of 5 years for equities included in additional tier 1; and

(B) Shall not redeem, revolve, cancel, or remove any equities included in additional tier 1 capital without prior approval of the FCA under paragraph (f) of this section.

* * * * *

(d) * * *

(1) * * *

(i) The instrument is issued and paid-in;

* * * * *

(viii) * * *

(C) The capital instruments are in excess of \$1,000.

* * * * *

(xi) The System institution's capitalization bylaws, or a resolution adopted by its board of directors under § 628.21, provides that the institution:

(A) Establishes a minimum call, redemption or revolvment period of 5 years for equities included in tier 2 capital; and

(B) Shall not call, redeem, revolve, cancel, or remove any equities included in tier 2 capital without prior approval of the FCA under paragraph (f) of this section.

* * * * *

(f) * * *

(5) * * *

(ii) After such cash payments have been declared and defined by resolution of the board, the dollar amount of the System institution's CET1 capital at quarter-end equals or exceeds the dollar amount of CET1 capital on the same quarter-end in the previous calendar year; and

* * * * *

14. Add § 628.21 to read as follows:

§ 628.21 Capital bylaw or board resolution to include equities in tier 1 and tier 2 capital.

In order to include otherwise eligible purchased and allocated equities in tier 1 capital and tier 2 capital, the System institution must adopt a capitalization bylaw, or its board of directors must adopt a binding resolution, which resolution must be acknowledged by the board on an annual basis in the capital adequacy plan described in § 615.5200, in which the institution undertakes the following, as applicable:

(a) The institution shall obtain prior FCA approval under § 628.20(f) before:

(1) Redeeming or revolving the equities included in common equity tier 1 (CET1) capital;

(2) Redeeming or calling the equities included in additional tier 1 capital; and

(3) Redeeming, revolving, or calling instruments included in tier 2 capital other than limited life preferred stock or subordinated debt on the maturity date.

(b) The equities shall have a minimum redemption or revolvment period as follows:

(1) 7 years for equities included in CET1 capital, except that the statutory borrower stock described in § 628.20(b)(1)(x) may be redeemed without a minimum holding period and that equities designated as unallocated retained earnings (URE) equivalents

cannot be revolved without submitting a written request to the FCA for prior approval;

(2) a minimum no-call, repurchase, or redemption period of 5 years for additional tier 1 capital; and

(3) a minimum no-call, repurchase, redemption, or revolvment period of 5 years for tier 2 capital.

(c) The institution shall submit to FCA a written request for prior approval before:

(1) Redesignating URE equivalents as equities that the institution may exercise its discretion to redeem other than upon dissolution or liquidation;

(2) Removing equities or other instruments from CET1, additional tier 1, or tier 2 capital other than through repurchase, cancellation, redemption or revolvment; and

(3) Redesignating equities included in one component of regulatory capital (CET1 capital, additional tier 1 capital, or tier 2 capital) for inclusion in another component of regulatory capital.

(d) The institution shall not exercise its discretion to revolve URE equivalents except upon dissolution or liquidation and shall not offset URE equivalents against a loan in default except as required under final order of a court of competent jurisdiction or if required under § 615.5290 in

connection with a restructuring under part 617 of this chapter.

(e) The minimum redemption and revolvment period (holding period) for purchased and allocated equities starts on the common cooperative equity issuance date, as defined in § 628.2.

15. Amend § 628.22 by revising paragraph (a)(6) and adding paragraph (b) to read as follows:

§ 628.22 Regulatory capital adjustments and deductions.

* * * * *

(a) * * *

(6) The System institution's allocated equity investment in another System institution or service corporation; and

* * * * *

(b) *Regulatory adjustments to CET1 capital.*

(1) Any accrual of a patronage or dividend payable or receivable recognized in the financial statements prior to a related board declaration or resolution must be reversed to or from unallocated retained earnings for purposes of calculating CET1 capital.

(2) [Reserved]

* * * * *

16. Amend § 628.32 by revising paragraph (1)(1) to read as follows:

§ 628.32 General risk weights.

* * * * *

(1) * * *

(1) A System institution must assign a 0-percent risk weight to cash owned and held in all offices of the System institution or in transit; to gold bullion held in the System institution's own vaults or held in a depository institution's vaults on an allocated basis, to the extent the gold bullion assets are offset by gold bullion liabilities; and to exposures that arise from the settlement of cash transactions (such as equities, fixed income, spot foreign exchange (FX), and spot commodities) with a central counterparty where there is no assumption of ongoing counterparty credit risk by the central counterparty after settlement of the trade.

* * * * *

17. Amend § 628.43 by revising paragraphs (d) (1) and (2) to read as follows:

§ 628.43 Simplified supervisory formula approach (SSFA) and the gross-up approach.

* * * * *

(d) * * *

(1) The System institution must define the following parameters:

$$K_A = (1 - W) \times K_G + (0.5 \times W)$$

(2) Then the System institution must calculate

K_{SSFA} according to the following equation:

$$K_{SSFA} = \frac{eau - e^{al}}{a(u - l)}$$

Where:

$$a = - \frac{1}{p \times K_A},$$

$$u = D - K_A,$$

$$l = \max(A - K_A, 0), \text{ and}$$

$$e = 2.71828, \text{ the base of the natural logarithm}$$

* * * * *

18. Amend § 628.52 by revising paragraph

(c)(2)(ii) to read as follows:

§ 628.52 Simple risk-weight approach (SRWA).

* * * * *

(c) * * *

(2) * * *

(ii) Under the variability-reduction method of measuring effectiveness:

$$E = 1 - \frac{\sum_{t=1}^T (X_t - X_{t-1})^2}{\sum_{t=1}^T (A_t - A_{t-1})^2}$$

Where:

$$\underline{X_t} = A_t - B_t;$$

$\underline{A_t}$ = the value at time t of one exposure in a hedge pair; and

B_t = the value at time t of the other exposure in
a hedge pair.

* * * * *

19. Amend § 628.63 by:

- a. Removing and reserving paragraph (b) (3);
- b. Revising paragraph (b) (4) .

The revision reads as follows:

§ 628.63 Disclosures.

* * * * *

(b) * * *

(4) A reconciliation of regulatory capital
elements using month-end balances as they relate to its
balance sheet in any applicable audited consolidated
financial statements. The reconciliation must include a
statement that compliance with the regulatory capital
requirements outlined in subpart B of this part is
determined using average daily balances for the most
recent 3 months.

* * * * *

Dated: September 16, 2021. Dale Aultman,
Secretary,
Farm Credit Administration Board.